Stout v. Commissioner, 71 T. C. 441 (1978); 1978 U. S. Tax Ct. LEXIS 5

Payments from a voluntary retirement pension do not qualify for the sick pay exclusion under IRC Section 105(d) if the recipient is not permanently disabled and retires voluntarily.

Summary

John E. Stout, a fireman with over 20 years of service, sought disability retirement but was deemed capable of light duty by three physicians. After his request for disability retirement was denied, Stout voluntarily retired and received a regular pension. The issue before the U. S. Tax Court was whether these pension payments qualified for the sick pay exclusion under IRC Section 105(d). The court held that they did not because Stout's retirement was voluntary and not due to a permanent disability that prevented all work. This ruling clarifies that voluntary retirement pensions, even for partially disabled individuals, are taxable and do not qualify for the sick pay exclusion.

Facts

John E. Stout, a fireman since October 18, 1951, applied for disability retirement from the Indianapolis Fire Department. Three physicians examined him and determined that while he was unable to engage in active firefighting, he could perform light duties. The fire chief denied his request for disability retirement. Stout then voluntarily retired on January 13, 1972, and began receiving a regular pension. For the year 1974, he received $5,074. 92 under protest and claimed a sick pay exclusion of $4,940. 40 on his federal income tax return, which was disallowed by the IRS.

Procedural History

Stout and his wife filed a joint federal income tax return for 1974. The IRS determined a deficiency of $430 and disallowed the claimed sick pay exclusion. Stout petitioned the U. S. Tax Court, which heard the case and issued its opinion on December 27, 1978.

Issue(s)

1. Whether the payments received by John E. Stout from the Indianapolis Fire Department's pension fund in 1974 qualify for the sick pay exclusion under IRC Section 105(d).

Holding

1. No, because the payments were from a voluntary retirement pension, not a disability pension, and Stout was not permanently disabled and unable to perform all work.

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Court’s Reasoning

The court analyzed whether Stout’s pension payments qualified for the sick pay exclusion under IRC Section 105(d) and the applicable regulations. The court noted that to qualify for the exclusion, payments must be received in lieu of wages for a period of absence due to personal injury or sickness. Stout’s voluntary retirement and the medical assessments indicating he was capable of light duty led the court to conclude that his pension was not a disability pension but a regular voluntary retirement pension. The court cited *Walsh v. United States* and *O’Neal v. United States* to support its view that voluntary retirement pensions are taxable and do not qualify for the sick pay exclusion. The court emphasized the distinction between voluntary retirement and disability retirement, stating, “In this case, the petitioner was not absent from work on account of personal injury or sickness. “

Practical Implications

This decision clarifies that voluntary retirement pensions do not qualify for the sick pay exclusion under IRC Section 105(d), even if the retiree is partially disabled but capable of some work. For legal practitioners, this means advising clients who are considering voluntary retirement to understand that their pension payments will be taxable unless they can demonstrate permanent disability preventing all work. Businesses and public sector employers should ensure clear distinctions in their pension plans between voluntary and disability retirement to avoid confusion and potential tax disputes. Subsequent cases, such as *Quarles v. United States*, have followed this precedent, reinforcing the principle that only payments directly linked to permanent disability qualify for the exclusion.

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